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MEMORANDUM FOR:

DCI

Herewith a NIC-produced draft paper, on recent world events, for your 8 September meeting with the PFIAB. It has been coordinated with the DDI. It confines itself to eight developments of greatest consequence to US interests -- since you last so briefed PFIAB (in May). The text is about 30 minutes worth, with a few additional mini-subjects should you wish to raise them.

Hal Ford
NIO/AL

Date

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THE DIRECTOR OF CENTRAL INTELLIGENCE

WASHINGTON, D.C. 20505

National Intelligence Council

3 September 1982

DCI Remarks to PFIAB, September 8, 1982,
on World Crises

I plan to highlight the principal events that have occurred in the world since mid-May, when I last reviewed such developments with you, and to indicate likely trends and their significance. I restrict this examination to those recent events of greatest consequence for US interests.

Soviet actions. There have been no significant changes in Soviet behavior in the past few months, nor any moderation in Soviet foreign policies. The USSR has experienced a setback in the Middle East, where it has been excluded from Lebanese events and has disappointed its Syrian friends. Moscow is suffering significant casualties in Afghanistan, yet not improving its control over the country. In Poland the lines between people and government are more clearly drawn than ever, the political stalemate continues, the economy stagnates, and the very difficult "Polish problem" continues unrelieved for Moscow. Meanwhile the Soviet economy grows at less than 2 percent a year -- half that planned -- and the ensuing social malaise is causing concern for Soviet leaders.

It is largely in realms other than Soviet, however, that crisis events have been most pronounced in the past few months. The most significant of these are the following.

1. Lebanon. The tragedy of Lebanon has been the event of greatest consequence. The evacuation of the various PLO factions from West Beirut has

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gone successfully, and the dispersal of the PLO offers new opportunities for constructive change. Nonetheless, considerable instability and bloodshed lie ahead in Lebanon. Armed action by competing militias will accompany the efforts of Lebanon's new president, Bashir Jumayyil, to expand his influence into predominately Maronite Christian areas of northern and central Lebanon now occupied by the Syrians. Many Sunni and Druze Muslims will continue to oppose Bashir's takeover, but will be too weak to stop him; the largest Muslim sect, the Shia, who predominate in the Israeli-occupied south, will probably continue to give Bashir their tacit backing. Israel will now turn its attention to pushing the remaining PLO fighters out of northern Lebanon and the Syrians and their Palestinian allies out of the Bekaa Valley. If diplomatic efforts fail, Israel is probably prepared to use force.

As for the PLO, it is undergoing a major transformation as it departs Beirut. No Arab state will offer the freedom to operate independently that Arafat enjoyed in Beirut. Syria in particular will seek to manipulate the large number of Palestinians evacuated to Damascus to serve Assad's interests. Arafat, moving to Tunis, will probably shuttle between Arab capitals, seeking to maximize his independence and to keep Arab attention focused on the Palestinians. We can expect him to capitalize on the Beirut aftermath. The moderate Palestinians led by Arafat will have a freer hand to pursue the political option. They are no longer controlled by Syria, and Arafat's prestige in the Arab world has never been higher. At the same time, the radical PLO groups, although small, will capitalize on the anti-US feeling and their hosts' rejectionist proclivities to engage in international terrorism against US and moderate Arab targets.

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The Lebanese crisis has clearly damaged Soviet prestige and interests in the Arab world, at least in the short term. Soviet military equipment has been widely criticized, and both Syria and the PLO feel strongly that Moscow failed to defend their interests. But the Soviets are continuing to rearm Syria, and over the longer term, Moscow may derive some benefit from the damage the Lebanese crisis inflicted on the US with certain Arab states.

US relations with the moderate Arabs -- especially Egypt -- were definitely shaken by the Lebanon crisis, and many leading Arab figures were convinced the US gave Israel approval for the invasion and engineered Bashir's election. Cairo temporarily put a freeze on some strategic projects, and said it would not rejoin the autonomy talks until Israel totally withdraws from Lebanon. More recently, President Reagan's new peace initiative has met a generally receptive -- though as yet equivocal -- response in the Arab world.

2. The Iran-Iraq war. Here several significant developments have arisen from this deadlocked struggle. Iraq has successfully withstood Iran's invasion and should be able to blunt additional Iranian offensives. In Baghdad, Saddam Husayn's position has been at least temporarily bolstered. In Tehran, Khomeini remains personally committed to continuing the war until Saddam is overthrown. Khomeini's internal position is strong, and there seem to be few political constraints preventing further Iranian offensive. The Iranian clerics are meanwhile steadily consolidating their grip on power and probably can now manage the transition of power when Khomeini dies. The greatest danger attending the Iran-Iraq war remains the possibility that hostilities might so expand that oil exports from gulf suppliers would be

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endangered. Iraq has attacked Iran's key oil facility at Khark Island, but so far with little success. Unless Baghdad can do better, Iran should be able to export between 1.5 and 2 million b/d. Iraq's oil exports, 700,000 b/d, all go through the Turkish pipeline now, since the Syrian pipeline is shut as part of Assad's effort to help Khomeini overthrow Saddam.

3. Mexico's financial distress. This crisis, the most severe of its kind since the 1910 revolution, threatens not only Mexico's stability but that of the international financial system. Mexico's foreign debt of over \$80 billion is the largest of any LDC. About \$25 billion of this debt is held in the US, and the 9 largest US banks have exposure equal to about one-half of their capital. Even if rescheduling proves successful, as seems likely, a number of severe problems will remain: (1) confidence in lending to LDCs will suffer, (2) Mexico will have to impose severe and painful austerity measures, (3) this will in turn stimulate political tensions; and (4) Mexico's new president, de la Madrid, will begin his term at a major disadvantage. Mexico's institutions appear sufficiently strong to weather the storm and avoid a major breakdown of the present political system -- although Lopez Portillo's recent actions -- and inactions -- are adding to the turmoil, and de la Madrid is himself an unknown factor.

4. New risks to the international financial system. LDC indebtedness has become enormous: between 1973 and 1981 it increased five-fold, surpassing \$500 billion, even though servicing it was not a major problem until 1981-82. The LDC debt has become a major problem as LDC exports have fallen, as interest costs have surged -- reaching 50 percent of exports for some major

LDCs, and, most recently, as Mexico's crisis has rattled bankers' confidence in the international financial system. In 1981, 28 LDCs were in arrears in debt servicing, but their aggregate bank-debt was less than two percent of the total; now, with Mexico in the process of rescheduling and Argentina to do so soon, the volume of debt subject to some form of relief has risen to nearly a quarter of the total LDC debt. Because of these problems, coincident with increasing bankruptcies in the industrial world, the international financial system is now more prone to a major crisis than at any time in the past 30 years. At a minimum, short of a major financial crash, these weaknesses will almost certainly cause many LDCs to curtail imports sharply and to reap heightened domestic political trouble. The resulting cuts in exports from industrial countries will in turn hinder their economic recovery.

5. The aftermath of the Falklands crisis. When we met in May the struggle for the Falklands had begun. I have directed the intelligence community to follow with especial care the principal effects of that crisis. These are the marked impetus which the crisis has given Argentine political and economic instability, and Argentine pursuit of an eventual nuclear weapons capability -- and the impact the crisis has had on numerous territorial disputes elsewhere in Latin America, and on the desire of countless states in the world to acquire high-technology weapons.

6. Central America. Here the primary development in the last few months has been a heightening of tensions along Nicaragua's borders and, in turn, a rise of internal disaffection with the Sandinista regime. There is in fact a greater regionalization of the conflict: not only Sandinista-backed insurgency

in El Salvador and Guatemala, and Nicaraguan and Cuban-backed terrorist operations in Honduras and Costa Rica, but a dramatic rise in violence along the Nicaraguan-Honduran border, including a doubling in the number of anti-Sandinista attacks within Nicaragua. There are no signs that the Nicaraguans are preparing a major cross-border offensive into Honduras, but prospects for Nicaraguan raids or strikes on anti-Sandinista camps there remain high.

In El Salvador the security situation has improved somewhat. The guerrillas will probably have to limit their activities in the near future mostly to sabotage, ambushes, or overrunning small towns. The political picture there remains fragile, marked by frictions and coup rumors, although the coalition government is still holding together. The economy continues to decline.

7. Pakistani nuclear weapons development. Recently acquired information details Pakistani plans for producing plutonium in violation of international non-proliferation safeguards -- suggesting that President Zia may soon be willing to authorize certain weapons development activities that could jeopardize the US-Pakistani security relationship if revealed. New evidence has also come to light of late -- though circumstantial and open to differing interpretation -- which suggests that the Chinese may be assisting Pakistan's nuclear weapons plans; if so, this could raise the potential for Indian nuclear weapons testing or preemptive military action against the Pakistani program.

8. The pipeline: 'This question has definitely introduced major frictions into US-European relations. The West Europeans will almost

certainly not reverse their intentions to participate in the construction of the Urengoy pipeline and to buy gas from it. It is nonetheless possible that they may come to scale down the amounts of gas they will purchase from the USSR in the future.

The pipeline question is meanwhile a good deal for the USSR in many respects: that is, cheap loans from the Western Europeans; potential earnings from gas sales of about \$5 billion annually in badly needed hard currency; increased Western European energy dependency on the USSR; and -- not least -- substantial new frictions in Europe's relations with the USA. Furthermore, the technical aspects of Soviet pumping capacity are such that the USSR will be able to deliver about 80 percent of the planned throughput with only about one third of the planned compressor capacity -- giving the Soviets great flexibility in case new problems develop or, as is now the case, in the face of any Western sanctions. Meanwhile I have directed the intelligence community to concentrate on finding out whether the Soviets are using prisoner labor to construct their pipeline. I will be reporting our findings to you.

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ADDITIONAL, SHORT ITEMS

Anti-American terrorism: There has already been a rise in attacks against US persons and interests, by various terrorist groups, since the Israeli incursion into Lebanon. More such attacks against American targets are probable, especially in Western Europe and the Middle East. Apart from Middle East events, terrorists and Salvadoran guerrilla groups operating in Honduras have greatly increased bombing attacks of late against US and Honduran targets. There has also been other terrorist activity elsewhere in Latin America. The outlook is for more.

Afghanistan: In addition to the military stalemate, there are new signs of jockeying within the Afghan Communist Party, and some signs of possible Soviet interest in imposing -- by coup -- still another "Afghan" regime upon the country.

Spain: Elections will take place in October, and the Spanish Socialists will probably emerge with at least a plurality. This will not mean a reversal of NATO membership, but the Socialists will be especially keen on getting beneficial arrangements out of Spain's integration to the military side of the Alliance. The enhanced influence of the Socialists will increase the chances of a coup attempt on the part of military elements.

Mozambique: Here there is danger that the Machel regime, increasingly threatened by a South African backed insurgent movement, may ask Cuba for troops to reverse the situation. We have no evidence that Machel has made such a decision, but were he to do so, the introduction of Cuban troops could have an inflammatory effect on the southern African scene.

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Somalia: Siad's position has weakened as a result of Ethiopian military pressure, a further weakening of the economy, and regional tribal rivalries. Siad still appears to have the support of key military leaders, who would probably remain anti-Soviet in a succession situation. But in the event they perceived that US aid was insufficient to cope with the Ethiopian menace, they would seek arms more vigorously from other suppliers -- e.g., Western Europe and Egypt -- and might even threaten the US-Somalia access agreement, in hopes of pressuring the US to be more forthcoming.

Egypt: Mubarak's credibility has suffered because of embarrassment over Lebanon and his failure to produce a new economic strategy. Still in control for now, his long term outlook is more questionable. The events of Lebanon have also sparked considerable criticism of the US; this will probably continue for some time.

South Africa-Angola: South African troops are continuing their operations in southern Angola. Their activities there may strengthen the hand of hardliners in Luanda who are opposed to a Cuban troop withdrawal, and thus complicate US efforts to negotiate an end of the Namibian problem.

Peru: There has been a recent surge in terrorist activity here, mostly on the part of a small Maoist organization which lacks popular and foreign support. President Belaunde so far has not committed the armed forces to counter-terrorist operations, fearing that in such circumstances the army might once again oust him.

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